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(3/02)

United States Government

Department of Energy

Oak Ridge Office

memorandum

DATE: October 12, 2007

REPLY TO ATTN: FM-712:Smith

SUBJECT: **FISCAL YEAR 2007 MANAGEMENT REPRESENTATION LETTER – OAK RIDGE OFFICE**

TO: Dr. Raymond Orbach, Under Secretary for Science, SC-1, FORS
Steven J. Isakowitz, Chief Financial Officer, CF-1, FORS

Obtaining a representation regarding the fair presentation of the Oak Ridge Office (ORO) financial statements is a significant procedure in the audit of those statements. As Manager of the ORO, I confirm that I am responsible for the fair presentation of the ORO statements, in conformity with principles generally accepted in the United States of America (U.S.). This letter covers all activities under the ORO allotment which includes: the East Tennessee Technology Park (ETTP) operated by Bechtel Jacobs Company LLC; the Oak Ridge Institute for Science and Education operated by Oak Ridge Associated Universities; the Oak Ridge National Laboratory operated by UT-Battelle, LLC; the Stanford Linear Accelerator Center operated by Stanford University; the Pacific Northwest National Laboratory (PNNL) operated by Battelle Memorial Institute; and the Thomas Jefferson National Accelerator Facility operated by Jefferson Science Associates, LLC.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

In connection with your audit of the Department's September 30, 2007, financial statements and its September 30, 2006, consolidated balance sheet, I confirm, to the best of my knowledge and belief, the following representations made to you and, where applicable, to KPMG:

1. The ORO consolidated financial statements of the Department are fairly presented in accordance with the Office of Management and Budget (OMB) requirements and in conformity with accounting principles generally accepted in the U.S.

2. ORO has made available to you and to KPMG:

    a. All financial records and related data.

b. If applicable, communications from OMB concerning noncompliance with or deficiencies in financial reporting practices.

3. ORO is responsible for compliance with applicable laws and regulations and has disclosed all instances of noncompliance with laws and regulations. In addition, ORO is responsible for the identification of and compliance with all aspects of applicable laws, regulations, contracts, or grants that could have a direct and material effect on the determination of consolidated financial statement amounts in the event of noncompliance and has disclosed all instances of noncompliance with laws, regulations, contracts, or grants.

4. ORO has complied, in all material respects, with applicable laws, regulations, and contracts and grants that could have a material effect on the consolidated financial statements in the event of noncompliance.

5. I acknowledge responsibility for the design and implementation of programs and controls to prevent, deter and detect fraud. I understand that the term "fraud" includes misstatements arising from fraudulent financial reporting and misstatements arising from misappropriation of assets. Misstatements arising from fraudulent financial reporting are intentional misstatements, or omissions of amounts or disclosures in financial statements or performance results to deceive financial statement users. Misstatements arising from misappropriation of assets involve the theft of the Department's assets where the effect of the theft causes the consolidated financial statements not to be presented in conformity with United States generally accepted accounting principles.

6. Except as disclosed to you, there have been no known:

   a. Instances of fraud, or suspected fraud, whether or not material, involving management or other employees who have a significant role in internal control over financial reporting, or others where the fraud could have a material effect on the financial statements.

   b. Instances of fraud, or suspected fraud, involving others (e.g., recipients of Federal financial assistance or other Federal payments) that could have a material effect on the consolidated financial statements.

   c. Allegations of fraud or suspected fraud affecting the Department received in communications from employees, former employees, regulators or others.

   d. Communications from other governmental entities or agencies (e.g., the U.S. Department of the Treasury) concerning noncompliance with, or deficiencies in, financial accounting practices.

e. Communications from regulatory or oversight agencies such as OMB and the Government Accountability Office (GAO), concerning noncompliance with, or deficiencies in, financial reporting practices that could have a material effect on the consolidated financial statements.

f. Violations, or possible violations, of laws or regulations whose effect should be considered for disclosure in the consolidated financial statements or as a basis for recording a loss contingency, except for unresolved recommendations in prior Office of Inspector General (OIG) and GAO audit reports, which have been considered in preparing the consolidated financial statements, and those items noted in the Independent Auditors' Report.

g. Violations or possible violations of specific requirements of contracts, grants, and budgetary procedures, the effects of which should be considered for disclosure in the consolidated financial statements or as a basis for recording a loss contingency, except for those items which have been considered in preparing the consolidated financial statements.

h. Allegations, either written or oral, of misstatements or other misapplications of accounting principles in the ORO consolidated financial statements.

i. Allegations, either written or oral, of deficiencies in internal control that could have a material effect on the ORO consolidated financial statements.

j. Communications from the legal counsel reporting evidence of a material violation of law or breach of fiduciary duty or similar violation by the Department or any agent thereof.

k. False statements affecting the consolidated financial statements made to you, our OIG, or other auditors who have audited entities under our control upon whose work you may be relying in connection with your audits.

7. Except as disclosed to you in writing, there are no known:

a. Unasserted claims or assessments that our General Counsel or the Department of Justice General Counsel has advised us are probable of assertion and must be disclosed in accordance with the Statement of Federal Financial Accounting Standards No. 5, *Accounting for Liabilities of the Federal Government*, as amended.

b. Other liabilities or gain or loss contingencies that have not been accrued that are required to be accrued or disclosed by the Statement of Federal Financial Accounting Standards No. 5, *Accounting for Liabilities of the Federal Government*, as amended.

c. Material transactions (e.g., obligations or commitments) or events that have not been properly recorded in the accounting records underlying the consolidated financial statements.

d. Events that have occurred subsequent to September 30, 2007, and through the date of this letter, that would require adjustments to or disclosure in the consolidated financial statements, Management's Discussion & Analysis (MD&A) (including performance measures), Required Supplementary Information (RSI), and Required Supplementary Stewardship Information (RSSI).

8. The Department indemnifies its management and operating contractors against financial responsibility from nuclear accidents, under the provisions of the Price-Anderson Act. Except to the extent otherwise disclosed in the Legal Representation Letter and in the Non-Monetary Loss contingency Report submitted to the OIG by the Department's program offices, I am aware of no liabilities or loss contingencies resulting from this indemnification at this time. However, in fiscal year (FY) 2007 two non-compliance incidents occurred at PNNL that have the potential for future legal action against DOE or potential loss contingencies.

9. The following have been properly recorded or disclosed in the consolidated financial statements:

a. Purchase commitments for inventory quantities in excess of normal requirements or at prices in excess of the prevailing market prices.

b. Changes in accounting principles affecting consistency. During FY 2007, the Department changed its methods of accounting and reporting for pension and other actuarial liabilities to adopt the provisions of Statement for Financial Accounting Standards No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans.*

c. Agreements to repurchase assets previously sold including sales with recourse.

d. The existence of and transactions with joint ventures and other related organizations.

e. Guarantees (for example, loan guarantee programs), whether written or oral, under which the Department is contingently liable.

f. Commitments for purchases of services or assets at prices involving material probable losses.

g. Losses to be sustained as a result of other than temporary declines in the fair value of investments.

h. Losses to be sustained in the fulfillment of, or from the inability to fulfill, any sales commitments.

10. Except as noted, there are no significant deficiencies in the design or operation of internal controls which could adversely affect the Department's ability to record, process, summarize and report financial data, and we have identified no material weaknesses in internal controls. In our Federal Managers' Financial Integrity Act (FMFIA) of 1982 assurance statement, I disclosed to you all significant deficiencies in the design or operation of internal controls which could adversely affect the Department's ability to process, summarize, and report financial data and identified no material weaknesses in internal control. We interpret "significant deficiencies in the design or operation of internal controls" to be consistent with the concept of a "reportable condition" defined under standards established by the American Institute of Certified Public Accountants. Such standards define a "reportable condition" as a significant deficiency in the design or operation of internal control that could adversely affect the entity's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements. I understand that the term "material weakness in internal control" is a reportable condition for which the design or operation of one or more internal control components does not reduce to a relatively low-level risk that errors or fraud in amounts that could be material in relation to the financial statements may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

11. ORO has identified and properly accounted for all nonexchange transactions.

12. Except as disclosed in the consolidated financial statements, the Department has no plans or intentions that may materially affect the carrying value or classification of assets and liabilities. I have disclosed in the footnotes to the consolidated financial statements that future decisions, including but not limited to changes in environmental cleanup standards or remediation technologies, decisions to dispose of nuclear materials, revisions in land use or waste disposal assumptions, or reductions in Federal Government spending, could have a material effect on environmental remediation liabilities. The Department will ascertain the impact on the environmental remediation liabilities once we have some assurance that a policy, decision, or assumption is likely to be altered and make any necessary adjustments or disclosures in future consolidated financial statements.

13. Inventories and operating materials are stated at historical cost in accordance with Statement of Federal Financial Accounting Standards No. 3, *Accounting for Inventory and Related Property*, except where valuation at net realizable value is authorized by the Statement. Exceptions include (1) stockpile materials that management has determined have permanently declined in value below cost or are damaged or decayed, and (2) excess, obsolete, or unserviceable items. Where feasible, physical counts and measurements of inventories and operating materials were made, and records were

appropriately adjusted to reflect the physical inventories. The Department's inventory of nuclear materials is valued at standard transfer value, which approximates historical cost, except for certain nuclear materials that have been identified as surplus or excess to the Department's needs. These nuclear materials are recorded at their net realizable value. Capitalization of costs associated with the stockpile life extension program, the tritium production program and the plutonium pit production are not applicable to ORO.

14. I believe that the carrying amounts of all material assets are recoverable. We understand that with respect to the majority of the Department's assets, including nuclear materials and plant and equipment, the term "recoverable" does not imply that the Department can or would recoup the assets' carrying values by selling them, but that the assets are fulfilling their intended purposes and that their serviceability has not been impaired or that any material impairments are reflected in reduced carrying values for the assets.

15. ORO has satisfactory title to all owned assets and there are no liens or encumbrances on such assets nor have any assets been pledged as collateral. The Department has commitments to the United States Enrichment Corporation (USEC) for the following leases: the Gaseous Diffusion Facilities located in Paducah, Kentucky and Portsmouth, Ohio; the Gaseous Centrifuge Enrichment Project located in Portsmouth, Ohio; and the Centrifuge (K-1600) Lease at ETTP located in Oak Ridge, Tennessee.

16. ORO has not, directly or indirectly, including through a component entity, extended or maintained credit, arranged for the extension of credit, or renewed an extension of credit in the form of a personal loan to or for any management member of the Department.

17. ORO has properly accounted for all property, plant, and equipment sold, destroyed, abandoned, or considered to be obsolete and to have no further use. ORO has also properly accounted for property, plant, and equipment predominately used in environmental remediation activities.

18. All capital assets are properly categorized as either work-in-progress or completed projects as required in the Department's policy. Further, all capital assets are properly capitalized, reported and, if applicable, depreciated.

19. ORO and its contractors have properly accounted for all internal use software that is used to operate programs and produce goods and services, as required, by Statement of Federal Financial Accounting Standards No. 10, *Accounting for Internal Use Software*. Capitalized internal use software costs are limited to those costs incurred after the completion of conceptual formulation, design, and testing of possible software project alternatives. The ORO and its contractors have capitalized labor costs for employees that worked on software development projects for a substantial portion of time.

20. ORO has performed the necessary procedural requirements to develop and support the deferred maintenance estimate reported in the disclosure required by Statement of Federal Financial Accounting Standards No. 6, *Accounting for Property, Plant, and Equipment*, as amended. All estimates developed for purposes of reporting the ORO's deferred maintenance levels were developed in accordance with Departmental guidance. These estimates are properly documented and readily verifiable.

21. Provisions, when material, have been made:

    a. To reduce excess, obsolete, damaged, or unusable inventories to their estimated net realizable value. For example, ORO has analyzed all of its nuclear materials and identified all such materials that are excess to ORO's needs and recorded appropriate allowances to record such inventories at net realizable value.

    b. For any material adjustments of long lived assets as a result of permanent impairment, in accordance with Statement of Federal Financial Accounting Standards No. 6, *Accounting for Property, Plant, and Equipment*, as amended.

22. Contractor receivables reported in the consolidated balance sheet represent valid claims for sales or other charges arising on or before the balance sheet date, and have been appropriately reduced to their estimated fair value.

23. Related party transactions, including sales, purchases, loans, transfers, leasing arrangements, guarantees, ongoing contractual commitments, and accounts receivable or payable to related parties, have been properly recorded and disclosed in the consolidated financial statements. I understand that the term "related party" refers to affiliates of the Department or its contractors; trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of management; key administrative, financial and legislative personnel and other members of the Department's management or businesses they represent or in which they have an interest; members of the immediate families of the Department's management; and other parties with whom the Department may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests. Another party is also a related party if it can significantly influence the management or operating policies of the transacting parties or if it has an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests.

24. During the FYs ended September 30, 2007, and 2006, ORO did not exceed its Congressionally-approved budgetary authorities.

25. All significant estimates, uncertainties, and material concentrations of risk known to management have been properly recorded and/or disclosed in the consolidated financial statements. Significant estimates are as of the balance sheet date, and could change materially within the next year. Concentrations refer to volumes of reimbursable work, revenues, available sources of supply, or markets or geographic areas for which it is reasonably possible that events could occur which would significantly disrupt normal operations or financing sources within the next year.

26. All sales transactions entered into by ORO are final and there are no side agreements with customers, or other terms in effect, which allow for the return of items sold, except for defectiveness or other conditions covered by the usual and customary warranties.

27. I believe that the actuarial assumptions and methods used to measure actuarial liabilities and costs of contractor employee pension and post-retirement benefit plans for financial accounting purposes are appropriate in the circumstances.

28. I have provided background and detailed cost information for all environmental liabilities identified to date, as well as information regarding pending, threatened, or unasserted claims related to the environmental project sites identified. Provision has been made for any material loss that is probable from remediation liabilities and liabilities for post-remediation stewardship associated with Department-owned properties, formerly utilized sites, and sites with uranium mill tailings. Recorded environmental remediation and stewardship liabilities are based on the Department's best and most recent estimates of the expected costs, stated in FY 2007 dollars, to remediate legacy facilities and contaminated sites managed by the Office of Environmental Management (EM) or other programs, perform long-term post-remediation stewardship activities; remediate active and surplus facilities managed by other programs, dispose of surplus nuclear materials and unneeded materials and chemicals. I believe that such estimates are reasonable based upon available information and that the liabilities, related loss contingencies, and the expected outcome of uncertainties have been adequately disclosed in the consolidated financial statements and related footnotes. The environmental remediation liability includes adequate provisions for costs to dispose of all nuclear materials and other unneeded materials and chemicals whose disposition as waste is probable (more likely than not) as defined by Statement of Federal Financial Accounting Standards No. 5, *Accounting for Liabilities of the Federal Government,* as amended. I have made a reasonable effort to identify the presence or likely presence of potential environmental contamination at Department-owned properties, and to identify formerly utilized sites and sites with uranium mill tailings for which the Department will be responsible for post-remediation stewardship.

29. The environmental remediation liability for facilities and sites managed by EM (EM liability) is based partly upon an accelerated cleanup approach. Achievement of accelerated cleanup goals is contingent upon receipt of anticipated funding. I believe the funding assumptions are reasonable.

30. EM cost estimates with respect to shipments of high-level waste and spent nuclear fuel are not applicable to ORO.

31. I agree with the findings of specialists preparing cost estimates for environmental remediation projects and disposal of wastes and surplus or unneeded materials, measuring employee retirement and postretirement benefit obligations, and measuring and sampling inventories of nuclear materials, and have adequately considered the qualifications of the specialists in determining the amounts and disclosures used in the consolidated financial statements and underlying accounting records. I did not give or cause any instructions to be given to specialists with respect to the values or amounts derived in an attempt to bias their work, and I am not otherwise aware of any matters that have had an impact on the independence or objectivity of the specialists.

32. The liability for spent nuclear fuel litigation is not applicable to ORO.

33. Costs have been recorded in accordance with the Statement of Federal Financial Accounting Standards No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government.*

34. Pursuant to the FMFIA, I have assessed the effectiveness of the Department's internal control in achieving the following objectives:

    a. Reliability of financial reporting - transactions are properly recorded, processed and summarized to permit the preparation of consolidated financial statements, MD&A, RSI and RSSI, in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition;

    b. Compliance with applicable laws and regulations - transactions are executed in accordance with: (i) laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the consolidated financial statements, and (ii) any other laws and regulations and government-wide policies that the OMB, Departmental management, or the OIG have identified as being significant and for which compliance can be objectively measured and evaluated.

35. Except as disclosed, all internal controls are operating as of September 30, 2007, and for the year then ended, in accordance with applicable policies and procedures and are effective in meeting the FMFIA objectives set forth above.

36. I have assessed the financial management systems to determine whether they comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. My assessment was based on guidance issued by OMB.

37. The financial management systems complied substantially with Federal financial management systems requirement and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2007.

38. ORO has properly accounted for all liabilities and commitments to the USEC under the lease agreements between the U.S. Department of Energy and USEC for the following leases: the Gaseous Diffusion Facilities located in Paducah, Kentucky and Portsmouth, Ohio; the Gaseous Centrifuge Enrichment Project located in Portsmouth, Ohio; and the Centrifuge (K-1600) Lease at ETTP located in Oak Ridge, Tennessee.

39. In accordance with *Government Auditing Standards*, I have identified to you the significant findings and recommendations from previous financial audits, attestation engagements, performance audits, and other studies related to the objectives of this audit and have accurately communicated to you the related corrective actions taken to address the findings.

If you have any questions or require further information, please feel free to contact me at (865) 576-4444 or Judith Penry, of my staff, at (865) 576-4446.

Gerald G. Boyd
Manager

cc:
G. J. Malosh, SC-3, FORS
T. M. Garnand, CF-1.2, GTN
G. S. Podonsky, HS-1, GTN
D. R. Spurgeon, NE-1, FORS
J. A. Rispoli, EM-1, FORS
R. J. Brown, M-3, ORO
M. J. Weis, SC-PNSO
P. M. Golan, SC-SSO
J. A. Turi, SC-TJSO